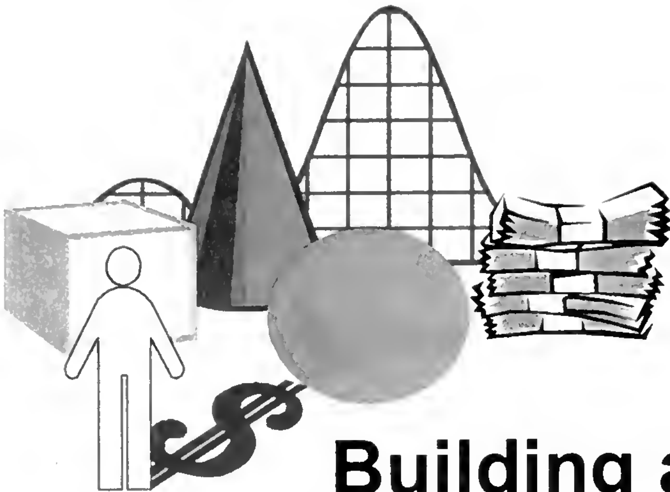


Building a Better Tax Structure

Tax Reform Proposal

Governor Marc Racicot
November, 1998

Vision for Montana's Tax Structure

This tax reform proposal is designed to improve Montana's tax structure. The vision for Montana's tax structure is based upon:

- Establishing and following the guiding principles of taxation;
- Having a balanced tax structure;
- Ensuring the tax burden for individuals and businesses is balanced and reasonable;
- Generating the same level of revenue as is currently being generated;
- Establishing and maintaining a respectful financial relationship between state and local governments by providing complementary funding laws and revenues.

Universal Guiding Principles for Taxation

Taxation should be:

- Stable - *produce adequate and relatively constant revenue*
- Equitable – *treat individuals and businesses fairly*
- Economically Neutral – *does not interfere with private economic decisions in the marketplace*
- Simple – *easy for taxpayers to understand and minimize compliance costs*
- Complementary – *all economic activity and wealth contribute proportionally to support government services, and there is an appropriate funding relationship between state and local taxing jurisdictions*
- Balanced – *rely on a diverse and broad based range of revenue sources and tax types*
- Accountable – *tax law should be explicit, not hidden; proposals for change should be well publicized to stimulate debate*

What is a Balanced Tax System?

Most states' tax systems seek balance among sources and tax types to ensure stable revenue. States also desire to avoid a concentration of tax burdens on a few sources, which can make tax rates distort economic behavior.

Generally, balance in a tax system means that: many different tax bases are used; taxes are broad-based with a minimum of exclusions and deductions; tax rates are lower, resulting in less distortion of economically efficient decisions; revenue is less volatile; tax adjustments can be made in small increments with minimal economic and administrative disturbance; and taxes do not affect significant business decisions.

Tax systems are often thought of as three-legged stools with taxes on property, sales and income constituting the three legs. The stool is most steady when the three legs are in equal, or nearly equal, proportion.

Overview of Tax Reform Proposal

Property Tax Reform
- Reduce the property tax rate for Class 3 (agricultural land) and Class 4 (real commercial property, residential property) from 3.816% to 3%
- Provide residential property tax relief through a homestead exemption
- Eliminate all property taxes on business equipment, plus eliminate the livestock tax and railcar tax
- Reduce the Class 9 centrally assessed property tax rate
- Reduce property tax rate for railroads and airlines

Income Tax Reform
- Simplify and reduce individual income taxes; provide a tax credit for households earning under $50,000

Natural Resource Tax Reform
- Simplify and reduce oil and natural gas production tax rates

Additional Tax Reform
- Convert the motor vehicle tax and new motor vehicle tax to a $25 flat fee
- Eliminate telephone license tax
- Eliminate inheritance tax
- Eliminate most tax incentives

Revenue Distribution System
- Streamline and simplify local government funding
- Streamline and simplify school funding

Replacement Revenue
- Implement a broad-based, business consumption tax with medical services exempted

Revenue Impact of Tax Reform Proposal

The following table shows the revenue impact of the tax reform proposal. It costs $373,250,000 to eliminate or reduce current taxes. The replacement tax, a business consumption tax, generates $425,000,000.

After allowing an exemption for medical services (which costs $49,750,000), eliminating some tax incentive credits and providing for administrative expenses, the proposal is revenue neutral.

Revenue Impact of Tax Reform Proposal

Revenues:		
Consumption Tax Revenue (4%)	$ 425,000,000	
Minus Medical Exemptions	$ (49,750,000)	
Eliminate Tax Incentives/Credits	$ 900,000	
Total Revenue		$ 376,150,000
Expenditures:		
Property Tax Reform:		
Eliminate Business Equipment Tax	$ 125,100,000	
Eliminate Class 6 - Livestock Tax	$ 8,000,000	
Eliminate Carline Tax	$ 2,100,000	
Implement a Homeowner Exemption	$ 73,900,000	
Keep Timber Property Tax Constant	$ 3,700,000	
Oil & Gas Simplification	$ 3,700,000	
Eliminate Inheritance Tax	$ 11,000,000	
Individual Income Tax Reform	$ 51,050,000	
Convert Motor Vehicle Tax to Flat Fee	$ 88,200,000 *	
Eliminate Telephone License Tax	$ 6,400,000	
Total Expenditures		$ 373,150,000
Administrative Costs		3,000,000
Net Revenue		$ 0

*Additional work is necessary to formulate more accurate numbers.

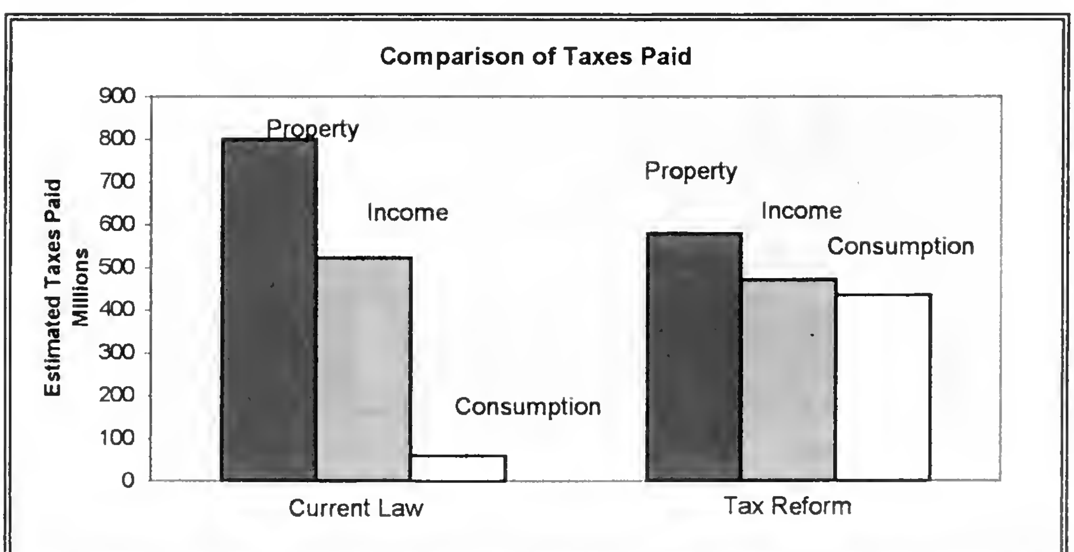
Comparison of Tax Reform Proposal to Current Tax System

Tax and revenue systems are often thought of as having three primary revenue sources: property tax, consumption tax, and income tax. Generally the three sources should be approximately equal. There are many other sources of taxes, which are also significant, but not included in the three primary revenue sources shown below. These are gas tax, natural resource taxes, fish and game license revenue, etc. The amount of property taxes, income taxes and consumption taxes paid under Montana's current tax system (column 1) and under the tax reform proposal (column 2) are shown in the following table.

Estimated Taxes Paid
(millions)

	Current Law	Tax Reform
Property	800.541	580.305
Income	522.089	471.939
Consumption	65.771	434.921

The following graph shows a comparison of property taxes, income taxes and consumption taxes paid under Montana's current tax system and under the tax reform proposal.



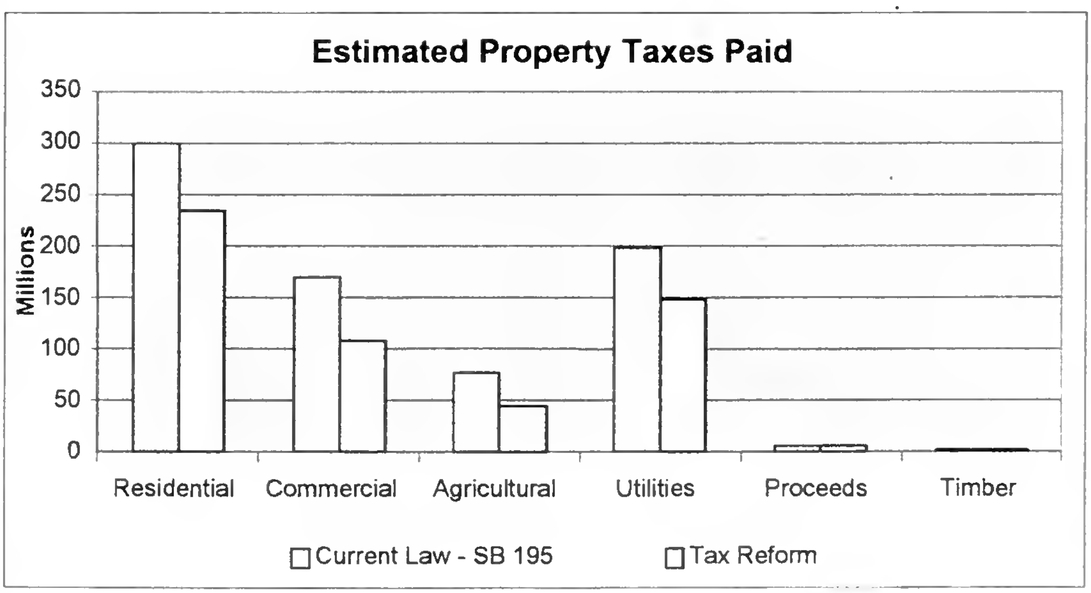
Tax Reform Proposal

Property tax reform is proposed for 99% of the current property taxes paid. As shown below after implementing full reappraisal, residential property will have a property tax reduction from fiscal year 1998 levels of 21.5%; commercial property tax reductions will be 36.0%; agricultural property tax reductions will be 41.7%; and utility property tax reductions will be 24.6%. Proceeds and timber property will maintain the current level of property tax.

Comparison of Property Taxes Paid in Fiscal Year 1998 to Tax Reform Proposal

Estimated Property Taxes Paid

	Current Law	Tax Reform	Dollar Change	% Change
Residential	299,166,252	234,848,638	-64,317,614	-21.5%
Commercial	169,279,447	108,338,133	-60,941,314	-36.0%
Agricultural	77,078,426	44,955,027	-32,123,399	-41.7%
Utilities	197,793,303	149,130,609	-48,662,694	-24.6%
Proceeds	5,954,006	5,954,006	0	0.0%
Timber	2,864,288	2,864,288	0	0.0%
Total	752,135,722	546,090,701	-206,045,021	-27.4%



- **Reduce property tax rate for agricultural land, real commercial property and residential property**
  The tax rate is reduced from 3.816% to 3% for Class 3 (agricultural land) and Class 4 (real commercial property and residential property).

- **Provide residential property tax relief through a homestead exemption**
  A homestead exemption – a program which exempts from taxation a portion of the market value of residential property – will provide property tax relief to Montana homeowners. An exemption of 40% of the first $200,000 of the residence's market value is provided for all residential property.

- **Eliminate business equipment taxes**
  All business equipment tax is eliminated in every class. Mileage property such as railroad lines, transmission lines and pipelines are considered real property, not business equipment. The classes of property that have business equipment taxes eliminated are shown below:

  Class 5 – Pollution control equipment
  Class 6 – Rental equipment under $5,000
  Class 7 – Small telephone company equipment
  Class 8 – Business equipment
  Class 9 – Utility equipment
  Class 12 – Railroad and airline equipment

  Research shows many states exempt business equipment from property tax, and those states that do tax business equipment do so at a lower rate than Montana. Exempting business equipment from property tax will alleviate the property tax expenses for large and small businesses and will reduce reporting requirements.

  For the specific revenue impacts of eliminating business equipment taxes, see the table below.

Revenue Impact of Exempting Business Equipment

Class	Description		Est. Revenue Loss
5	Pollution Control	$	7,000,000
6	Rental Equipment Under $5,000	$	100,000
7	Small Telephone	$	200,000
8	Business Equipment	$	71,100,000
9	Utilities	$	45,700,000
12	Railroads and Airlines	$	1,000,000
Total		**$**	**125,100,000**

- **Eliminate property tax on livestock**
  This proposal eliminates property tax on livestock because livestock is very similar to business equipment.

- **Eliminate the carline tax**
  The carline tax on railcars is a substitute to the property tax. As railcars are considered business equipment, the carline tax is eliminated.

- **Reduce Class 9 centrally assessed tax rate**
  The property tax rate on real property is reduced from 12% to the exact percent that will keep the total Class 9 taxable value constant while maintaining the average annual growth rate of approximately 2% a year. This change will occur in the year in which the generation assets are reassessed from the Montana Power Company sale. This adjustment will maintain the average annual growth rate while allowing the tax rate to decrease.

  Utilities entering the competitive market need a tax that will ensure a "level playing field." Montana's tax policy should ensure that state utility businesses entering a competitive environment are not disadvantaged by taxes that cannot be applied equally to all firms regardless of where the company providing the service is located.

- **Reduce property tax rate for railroads and airlines**
  Class 12 railroads and airlines will have a tax rate reduction due to the federal 4-R Act. The act requires that railroads and airlines be taxed at a rate equal to the average effective rate applied to all commercial and industrial property in the state. This proposal's elimination of business equipment property tax and the change in Class 4 and Class 9 property tax rates, will result in a reduction of the Class 12 property tax rate for railroads and airlines.

- **Simplify and reduce individual income taxes**
  Under this proposal, a taxpayer's Montana individual income tax will be tied to federal taxable income. This simplification by itself takes approximately 48,000 Montana households off the income tax rolls. Because nearly all married couples will file joint individual income tax returns under the proposal, the number of tax returns filed should decrease by over 100,000.

A new "household" tax credit will further reduce individual income taxes for households earning less than $50,000. This credit, which varies with the type of household and the number of dependent children in the household, is nonrefundable; that is, it cannot exceed the household's tax liability. The credit is gradually phased out for households with incomes between $25,000 and $50,000.

The base credit for married couple households is $500. The base credit for "head of household" households is set at 80% of this amount, or $400, and the base credit for single filer households is set at 60% of this amount, or $300. In addition, married couples and head of household filers are entitled to an additional tax credit of $100 for each dependent child living in the household.

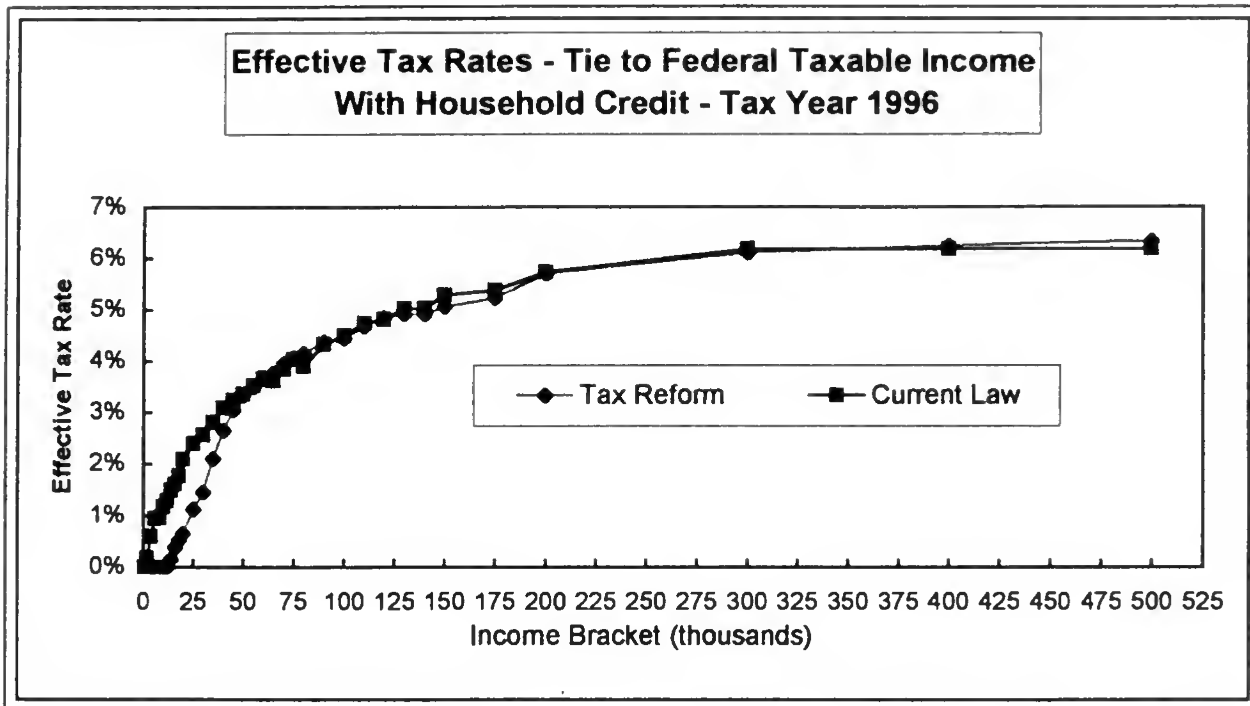
The credit acts to remove an additional 75,000 households from the tax rolls, resulting in a total of about 123,000 households being taken off the individual income tax rolls under the proposal.

The following table shows the income tax liability under current law and under the tax reform proposal. As shown the average tax reduction is 14% or $139. In total, tax liabilities are reduced for 238,000, or 66%, of the 360,000 total households.

Comparison of Current Law and Tax Reform Proposal - Individual Income Tax Liability
All Full-Year Resident Households

Income ($1,000s)	Number of Households	Current Law Liability	Tax Reform Liability	Change In Liability	Percent Change	Average Change
Less than $0	4,687	$0	$0	$0		$0
0 - 10	98,318	3,652,808	0	(3,652,808)	-100%	(37)
10 - 20	77,982	17,340,553	2,781,969	(14,558,584)	-84%	(187)
20 - 30	50,235	27,809,761	10,977,615	(16,832,146)	-61%	(335)
30 - 40	38,363	35,721,690	23,563,839	(12,157,851)	-34%	(317)
40 - 50	29,463	41,833,615	37,649,977	(4,183,638)	-10%	(142)
50 - 75	39,017	84,031,056	84,735,202	704,146	1%	18
75 - 100	11,344	39,168,395	40,474,908	1,306,513	3%	115
100 - 200	8,169	53,558,400	52,457,184	(1,101,216)	-2%	(135)
200 - 300	1,473	20,254,860	20,125,924	(128,936)	-1%	(88)
300 - 400	503	10,602,197	10,452,791	(149,406)	-1%	(297)
400 - 500	216	5,859,823	5,916,120	56,297	1%	261
Over 500	450	28,349,103	29,091,648	742,545	3%	1,650
Totals	**360,220**	**$368,182,261**	**$318,227,177**	**($49,955,084)**	**-14%**	**($139)**

The following graph compares the tax liability under current law to the tax reform proposal. The average household tax liability is reduced in all income brackets under $60,000; average tax liabilities are reduced in income brackets between $100,000 and $400,000 as well.



- **Simplify and reduce oil and natural gas production tax rates**
  Oil and gas production tax rates will be simplified from the current 36 tax rates to 8 tax rates. This will result in an estimated 7.4% tax reduction.

Oil and Natural Gas Production Tax Rates
Tax Reform Proposal

Production Type	Working Interest Rate	Royalty Rate
Horizontal 0-18 Mo	0.8%	15.1%
Vertical 0-12 Mo.	0.8%	15.1%
Post-99 Regular	10.0%	15.1%
Pre-99 Regular	12.8%	15.1%
Secondary	8.8%	15.1%
Tertiary	6.1%	15.1%
Stripper	10.0%	15.1%
Stripper Incentive	5.8%	15.1%

Five separate state and local production taxes on oil and natural gas existed prior to 1996 when they were consolidated into a single production tax. The new consolidated production tax simplified the tax system; however, it still has a complex set of rates and distributions depending on production types. Montana's current structure contains 20 different production types, having 36 different tax rates to be applied.

Oil production trends show that total oil production has decreased 48% since fiscal year 1986. Natural gas production has been much more stable since 1986, and total production actually increased by slightly less than 1%.

Oil and natural gas taxes received by local governments have correspondingly dropped with decreases in production. However, tax revenue has decreased even more due to lower prices and the move to flat tax rates instead of the former net proceeds property tax system. Overall, local oil and natural gas production taxes have decreased 69% between fiscal year 1986 and fiscal year 1998.

An industry tax burden study of oil and gas production showed Montana currently ranks among the highest in the nation in oil and natural gas production taxes. Comparison studies are difficult and views of the comparable tax burdens among states will vary. Regardless of tax structure, with the current low oil and natural gas prices, a tax rate reduction may result in any significant new drilling activity.

- **Convert motor vehicle tax to a flat fee**
  While specific details of this reduction are yet to be worked out, the plan is to reduce the vehicle tax for light cars and trucks, which now averages $153, to a $25 flat fee. The flat fee replaces all taxes and fees currently assessed at the time the vehicle is registered. These include the new car sales tax, property tax, license fee, additional registration fee, county option property tax, county computer system fee, highway patrol pension fee, weed control fee and junk vehicle fee.

- **Eliminate telephone license tax**
  The telephone company license tax is eliminated. Currently, gross income in excess of $250 per quarter derived from any telephone business conducted in the state is subject to a license fee of 1.8%.

  Elimination of the telephone company license tax will help ensure all participants in the telecommunication industry are taxed in an equivalent manner. The telephone company license tax dates back to 1937 and was last updated in the 1991 legislative session. The current law does not reflect new technology. In addition, there is uncertainty regarding what types of business

can be taxed under the current law. Thus there is unequal taxation for competing businesses.

- **Eliminate inheritance tax**

  The inheritance tax, paid by the recipient of any decedent's property or interest within Montana, is eliminated.

  While Montana's inheritance tax is eliminated, the estate tax is not eliminated. If Montana does not collect the estate tax, the federal government will receive these funds as Montana taxpayers will not have the state tax credit to offset federal estate taxes.

- **Eliminate most tax incentives**

  Surveys of business location decision-makers and statistical studies evaluating the importance of tax incentives as a location factor have predominately shown that tax incentives do not stimulate economic activity and create jobs in a cost-effective manner.

  Business tax incentives and credits proposed for elimination are:

  - Alternative Fuel Motor Vehicle Conversion Credit
  - Canola Seed Oil Processing Facilities Reduced Rate
  - College Contribution Credit
  - Electrolytic Reduction Facilities Reduced Rate
  - Employer Health Insurance Credit
  - Energy Conservation Investment Credit
  - Gasohol Producing Equipment Reduced Rate
  - Interest Differential Credit
  - Montana Capital Company Credit
  - New/Expanded Industry Reduced Rate
  - Pollution Control Equipment Reduced Rate
  - Recycling Credit
  - Value-added Machinery and Equipment Reduced Rate
  - Wind Energy Producers Credit

  Individual income tax credits proposed for elimination are:

  - Alternative Fuel Credit
  - College Contribution Credit
  - Employer Health Insurance Credit
  - Energy Conservation Credit
  - Historic Buildings Credit
  - Montana Capital Company Credit
  - Non-fossil Energy Credit

- Recycling Credit
- Wind-powered Generation Equipment Credit

- **Streamline and simplify local government funding and school funding**
The financial relationship that exists between the state and local governments is complex, with over 100 different revenue sources collected and distributed between the government entities. In addition, the collection and distribution of monies dedicated to school funding is also complex. As part of the tax reform proposal, the funding restrictions and transfers of funds among state and local governments, and schools will be simplified.

Working with the Department of Revenue, a group of local government and school officials have developed a vision for a complementary state and local funding structure. Their vision is:

We are dedicated to a partnership among state, county, city and school districts that is based on mutual trust and respect for local authority. This partnership will enable all governments to respond to the demands of their citizens in the 21st century through a mix of taxes and fees that is understandable, equitable, stable and adequate. The collection and distribution system for these taxes and fees will be simple, efficient, accurate and timely.

These groups are working on the revenue distribution systems and the specific funding restrictions that need to be changed. The final proposal introduced to the 1999 Legislature will include the recommendations from this group for long-term change in the distribution mechanism and the financial relationship between these government entities.

- **Implement a broad-based, business consumption tax**
Ultimately, the consumption tax chosen by Montanans will be the end product of extensive debate and work on the part of the executive and legislative branches of government as well as rapidly growing ranks of citizens genuinely interested in tax reform.

What is meant by a "consumption tax"? Generally, taxes levied at the point of sale/consumption either on the seller or the consumer are often described as consumption taxes. These include both general (wide application) and selective (very specific) sales taxes. While Montana does not presently have a general consumption tax, we do have a number of selective sales taxes such as:

- cigarette sales tax – $.18 per pack,
- "other tobacco products" tax – 12½% of wholesale invoice price,
- new motor vehicles sales tax – 1½% of factory list price,

- lodging facility use tax, sometimes known as the "bed tax" or the "accommodations tax" – 4% of the room charge.

These taxes are calculated based upon the unit purchased, unaffected by the price (such as the cigarette tax) or, more typically, based upon a fixed percentage of the selling price (such as the accommodations tax).

Most Common Types of Consumption Taxes

Business consumption (or value added) tax: This tax is levied on the seller and applies broadly to virtually all consumption within the jurisdiction levying the tax. It is often called a multistage tax because it is levied on all business sales but uses a more accurate mechanism to limit the tax on business inputs. This mechanism is what is called the "credit invoice method" and provides the business a dollar for dollar tax credit for the tax paid on business inputs. In this manner the potential for tax "pyramiding" – that is, levying a tax upon a tax – is minimized. While well established in the international arena, value added taxes are less common among the states. The state of Michigan implemented a value-added tax in the late 1970's but has by now, so modified the original enactment, that it no longer resembles the international version of the tax.

Gross receipts tax: This tax is levied on the sellers for the privilege of engaging in business in the state. Again the tax is collected by the seller and is levied as a percentage of business sales or gross receipts. The New Mexico gross receipts tax or the Washington business and occupation tax are examples of gross receipts taxes. The New Mexico tax for example, applies to all businesses registered and making taxable sales within that state. A method to allow for certain sales as non-taxable is provided to limit the taxation of business inputs or sales for export.

Retail sales tax: This tax is levied on the customer usually as an additional percentage of the sales price. The responsibility to collect the tax is normally on the seller and the tax applies to all customers, businesses and individuals alike, on their purchases of taxable items. The retail sales tax is the most common model among the other states.

Which of these forms of consumption tax is best for Montana?

This proposal recommends a model that will impose a 4% business consumption tax to be levied on all businesses within the state. The tax is broad based and is levied on the gross receipts from providing goods and services to consumers in Montana. The tax as proposed will have very few exemptions, most notably financial transactions, residential rentals, medical services, and the sale of an ongoing business. The proposal also includes a very sound mechanism to eliminate the consumption tax on business inputs.

This mechanism is called a credit invoice method that allows businesses a full and refundable credit for business consumption taxes paid and works to eliminate the tax pyramiding that is much more prevalent in the other consumption tax options. This model for a consumption tax was chosen because it will update Montana's tax structure for the future and better position Montana businesses to compete in the interstate and international markets. It also meets the following criteria that are essential elements against which all proposals should be measured.

- The tax base should be kept as wide as possible so the growth in revenue is proportionate to economic growth.

- The tax should be as absolutely simple as possible (statewide single rate, very few exceptions or exemptions). In this manner, the state will maximize the chances of sustaining a defense of the state's efforts to ensure that out of state businesses operate on a level playing field with Montana businesses.

- The tax should include a sales-threshold where sales activities above that level would allow Montana to assert jurisdiction over out of state sellers. This economic presence in the state, also called nexus, would require out of state sellers to comply with the provisions of the tax.

- To the best extent possible, the tax should not be levied against productive business inputs.

- Finally, the tax should be administratively simple.

The disadvantage of this tax is primarily attributed to the lack of familiarity with this method of taxation, although it is well known and used in the European Economic Community and elsewhere in the world.

What are the principal disadvantages to the other models?

Gross receipts tax: The principal disadvantage of the gross receipts tax is the inability to remove the tax on business inputs. The nontaxable procedures provided typically require the presentation of non-taxable transaction certificates. This process can be cumbersome and is subject to abuse.

Retail sales tax: The most significant disadvantages of the present models are their focus on taxing goods and not services with the resulting erosion of the tax base given the significant shifts in consumption moving toward services. As well, the tax has a significant potential for pyramiding. Attempts to fine-tune the low income impacts and the potential for pyramiding by allowing numerous deductions or exemptions adds complexity and undermines the equity and efficiency of the tax.

Administrative costs

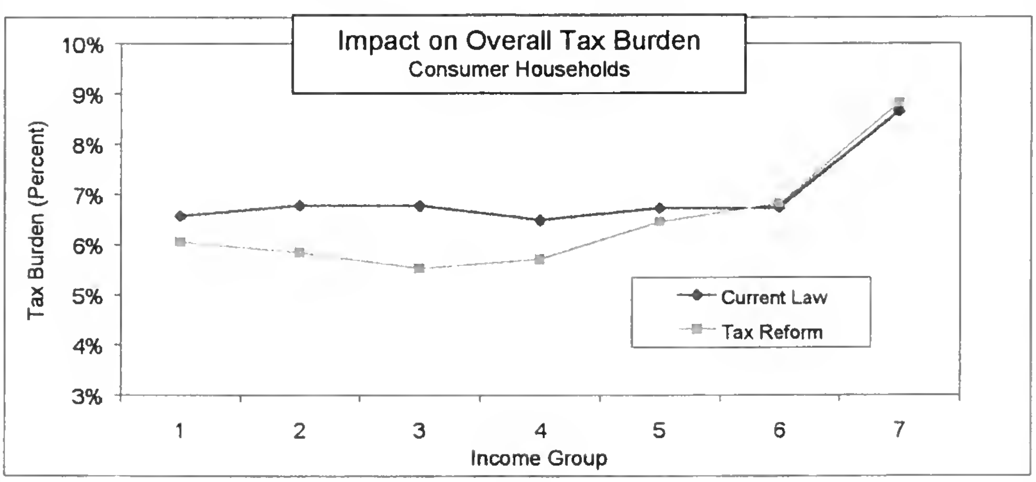
The administrative costs associated with this new proposal are expected to be a net increase above current level of \$3 million per year. The operating costs associated to the new business consumption tax are estimated to be approximately \$5.3 million per year, between 1% and 1½% of the revenues from the new tax. Concurrently, the reduction in Department of Revenue administrative expenses associated to the elimination and simplification of existing taxes is expected to save in the range of \$2.3 million per year. Therefore, the net ongoing cost is reflected as \$3 million.

Taxpayer Burden

The overall tax burden impact on consumer households under the proposed tax reform is shown in the following two charts. The difference between the two charts reflects a difference in the assumption regarding how businesses will respond to business property tax reductions. The overall tax burden reflects the combined tax paid for income tax, residential property tax, motor vehicle taxes, and the new business tax.

The first chart embodies the assumption that in a competitive environment a significant reduction in the property taxes paid by businesses should translate into reduced prices for the goods and services they sell. It shows the impact on the tax burden under the assumption that businesses pass through to households price reductions proportional to (1) the business equipment share of total business tax relief, and (2) the households' relative share of the total amount of new business tax. Under this assumption, the average tax burden for households in the first five income brackets would be reduced, while the average tax burden for households in the top two income brackets would change little.

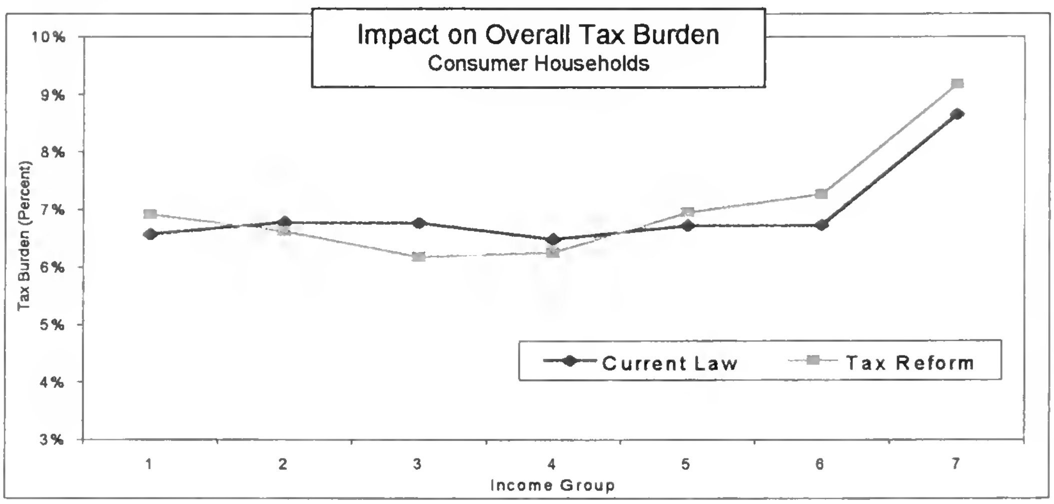
Overall Tax Burden - Current Law Vs. Tax Reform
Assumes Proportional Pass Through Of Property Tax Reductions In Consumer Prices



Income Group	Income Range	Current Law	Tax Reform
1	$10,000 - $14,999	6.56%	6.05%
2	$15,000 - $19,999	6.77%	5.84%
3	$20,000 - $29,999	6.76%	5.53%
4	$30,000 - $39,999	6.49%	5.71%
5	$40,000 - $49,999	6.72%	6.45%
6	$50,000 - $69,999	6.73%	6.82%
7	$70,000 plus	8.65%	8.82%

The second chart shows the change in relative tax burden under the assumption that businesses will not pass through any reduction in their property taxes in the form of price reductions. Under this assumption, the average tax burden for households in the 2nd, 3rd, and 4th income brackets would decrease slightly, while the average tax burden for households in the remaining income brackets would increase slightly.

Overall Tax Burden - Current Law Vs. Tax Reform
Assumes No Pass Through Of Property Tax Reductions In Consumer Prices



Income Group	Income Range	Current Law	Tax Reform
1	$10,000 - $14,999	6.56%	6.91%
2	$15,000 - $19,999	6.77%	6.62%
3	$20,000 - $29,999	6.76%	6.18%
4	$30,000 - $39,999	6.49%	6.25%
5	$40,000 - $49,999	6.72%	6.94%
6	$50,000 - $69,999	6.73%	7.26%
7	$70,000 plus	8.65%	9.17%

Appendix

Taxpayer Examples of Tax Burden Under Tax Reform Proposal

Tax Reform Proposal – Household Worksheet

Taxpayer Examples of Tax Burden Under the Tax Reform Proposal

The following pages show examples of how the overall tax burden would change for taxpayers and households under various scenarios. In preparing these examples, certain assumptions had to be made regarding particular circumstances for each taxpayer or household. These assumptions include the total income of the household, and how that income is divided between two-earner married couples; whether the household is renting or buying their own home; the value of the rental property or homeowner's property; and the number and value of vehicles owned by the household. (Also, an assumption has been made that in a competitive environment landlords will reduce their rents to accommodate the decreases in property taxes provided residential property under the proposal. These burden examples reflect the assumed rent reductions. However, actual rental reductions may take time.)

In calculating the business consumption tax burden, specific calculations and/or certain assumptions were made regarding the total amount of household expenditures that would not be subject to the consumption tax. Specifically excluded per the tax reform proposal were calculated amounts for social security taxes, state income taxes, federal income taxes, automobile insurance, and home mortgage payments or rent.

Example 1: Married, Two Children, Income of $20,000; Renters
Example 2: Married, Two Children, Income of $50,000; Homeowners
Example 3: Married, Two Children, Income of $100,000; Homeowners
Example 4: Married Couple, Retired, Income of $30,000; Homeowners
Example 5: Single, Retired, Income of $8,000; Homeowner
Example 6: Single, Two Children, Income of $11,960; Renter
Example 7: Single, Income of $28,000; Renter

These examples are not intended to be all inclusive of the many circumstances Montana households may encounter. Nor are they intended to be precise calculations of the impact of this proposal. Instead, they provide practical examples of how the proposal may impact typical households, and provide a guide and example of how each taxpayer may determine how the proposal will impact his/her tax burden.

Tax Reform Proposal - Taxpayer Example 1

Household Description:
- Married Couple with Two Children
- Total Household Income of $20,000 (household income split 60%/40%)
- Renters
- One Auto Valued at $6,000

INCOME TAX

Current Law Tax

	Filer 1	Filer2
Total Income	$12,000	$8,000
Standard Deduction	(2,400)	(1,600)
Exemptions	(4,650)	(1,550)
Taxable Income	4,950	4,850
Tax Liability	140	136
Total Tax Liability		**$276**

Tax Reform

	Household
FAGI	$20,000
Federal Standard Deduction	(6,900)
Federal Exemptions	(10,600)
Taxable Income	2,500
Tax Liability Before Credit	100
Household/Dependent Credit	(700)
Tax Liability After Credit	**$0**

Change in Income Tax: **($276)**

PROPERTY TAX

Current Law Tax

Value of Rented Home	$68,600
Homestead Exemption (none)	0
Value Net of Exemption	$68,600
Taxable Valuation Rate	3.838%
Taxable Value	$2,633
Mill Levy	0.425
Tax Liability	**$1,119**

Tax Reform

Value of Rented Home	$68,600
Homestead Exemption	27,440
Value Net of Exemption	$41,160
Taxable Valuation Rate	3.000%
Taxable Value	$1,235
Mill Levy	0.425
Tax Liability	**$525**

Change in Property Tax/Rent: **($594)**

MOTOR VEHICLE TAXES

Current Law Flat Fee	$13
Current Law Property Tax (2% of $6,000)	120
Total Current Law Tax	$133
Liability under Proposed Tax Reform	$25
Change in Motor Vehicle Tax	**($108)**

CONSUMPTION TAX

Current Law Tax	$0
Total Income	$20,000
Estimated Non-Taxable Expenditures	7,487
Estimated Taxable Expenditures	$12,513
Tax Rate	4%
Change in Consumption Tax	**$501**

NET IMPACT OF TAX REFORM PROPOSAL ON HOUSEHOLD	**($478)**

Tax Reform Proposal - Taxpayer Example 2

Household Description:
- Married Couple with Two Children
- Total Household Income of $50,000 (household income split 60%/40%)
- Homeowner; House Valued at $90,000
- One Auto Valued at $15,000

INCOME TAX

Current Law Tax

	Filer 1	Filer2
Total Income	$30,000	$20,000
Itemized Deductions	(7,959)	(4,900)
Exemptions	(4,650)	(1,550)
Taxable Income	17,391	13,550
Tax Liability	810	561
Total Tax Liability		**$1,371**

Tax Reform

	Household
FAGI	$50,000
Federal Itemized Deductions	(10,287)
Federal Exemptions	(10,600)
Taxable Income	29,113
Tax Liability Before Credit	1,356
Household/Dependent Credit	0
Tax Liability After Credit	**$1,356**

Change in Income Tax: **($15)**

PROPERTY TAX

Current Law Tax

Value of Owned Home	$90,000
Homestead Exemption (none)	0
Value Net of Exemption	$90,000
Taxable Valuation Rate	3.838%
Taxable Value	$3,454
Mill Levy	0.425
Tax Liability	**$1,468**

Tax Reform

Value of Owned Home	$90,000
Homestead Exemption	36,000
Value Net of Exemption	$54,000
Taxable Valuation Rate	3.000%
Taxable Value	$1,620
Mill Levy	0.425
Tax Liability	**$689**

Change in Property Tax/Rent: **($780)**

MOTOR VEHICLE TAXES

Current Law Flat Fee	$13
Current Law Property Tax (2% of $15,000)	300
Total Current Law Tax	$313
Liability under Proposed Tax Reform	$25
Change in Motor Vehicle Tax	**($288)**

CONSUMPTION TAX

Current Law Tax	$0
Total Income	$50,000
Estimated Non-Taxable Expenditures	19,258
Estimated Taxable Expenditures	$30,742
Tax Rate	4%
Change in Consumption Tax	**$1,230**

NET IMPACT OF TAX REFORM PROPOSAL ON HOUSEHOLD	**$147**